

# State and Local Government Fiscal Position in 1980

THE State and local government surplus on a national income and product accounting (NIPA) basis was \$29 billion in 1980, up \$2 billion from the surplus in 1979. The increase in the surplus reflected a larger acceleration in receipts growth than in expenditures growth. It was the net result of a \$3 billion increase in the surplus of social insurance funds and a \$1 billion decline in the surplus of other funds. The other-funds surplus has declined each year since 1977, from \$10 billion to about \$2 billion in 1980.

## Receipts

State and local government receipts increased 9 percent in 1980, up from a 7½-percent increase in 1979, but below the increases of 10 percent or more registered in 1977 and 1978 (table 1). All categories of receipts recorded strong increases in 1980 except corporate profits tax accruals, which declined 8½ percent. General own-source receipts accelerated—from a 7½-percent to a 9-percent increase—despite the decline in corporate profits taxes. Major increases were in personal tax and nontax receipts (especially income taxes) and in indirect business tax and nontax accruals other than sales and property taxes, especially in receipts related to exploitation of mineral wealth.

Personal income tax growth accelerated in 1980 despite a deceleration in income growth. The 16-percent increase was in line with increases in recent years except 1979, when the increase was only 9 percent. The pattern appears to be related to that of net final settlements. In 1978, refunds exceeded payments on settlement by approximately \$1 billion; in 1979, the excess widened to about \$2.5 billion as a result of law changes affecting 1978 liabilities. The change of about \$1.5 billion from 1978 to 1979 accounted for much of the 1979 deceleration. In

1980, the excess was again about \$2.5 billion, so that final settlements had little effect on the change in personal income taxes.

Sales taxes, the largest category of indirect business taxes, again increased less than in the preceding year. Gasoline taxes declined slightly, despite a number of rate increases, as gasoline consumption declined for the second consecutive year. Factors contributing to the decline in consumption were an increasing proportion of more fuel-efficient vehicles in the fleet and a decline in the number of miles driven. General sales tax growth was held down by a number of law changes. Several States exempted some or all purchases of residential utilities from the sales tax base. Illinois and West Virginia continued a phased removal of food sold in grocery stores from the base, and Colorado removed these food sales from the base.

Business property taxes increased very slowly by historical standards—about 5 percent—but more than in 1978 and 1979. The virtual absence of growth

in 1978 and 1979 was largely the result of California's Proposition 13, which affected the second half of 1978 and all of 1979. By 1980, it no longer exerted a major negative effect on the year-to-year change. Tax limitations other than Proposition 13 enacted in 1978 are still slowing property tax growth. In addition, there are other possible reasons for continued slow growth: (1) Local officials may have found it prudent to limit tax growth in order to lessen pressures for voter initiatives, and (2) local governments that accumulated surpluses, as local governments as a whole did in 1977 and 1978, allowed tax growth to decelerate while accumulated balances ran down. In 1980, there were referendums in several States designed to restrict severely the growth of property taxes. However, these measures failed, with the exception of one in Massachusetts. This referendum required legislative implementation for several of its provisions, and both magnitude and timing of its property tax provisions are as yet unclear.

Table 1.—State and Local Government Receipts, NIPA Basis

	Calendar years								
	Billions of dollars					Percent change			
	1976	1977	1978	1979	1980	1977	1978	1979	1980
Receipts.....	267.8	298.0	327.4	351.2	383.4	12.3	9.9	7.3	9.2
General own-source receipts.....	187.1	206.4	225.6	242.6	264.2	11.4	9.2	7.6	9.0
Personal tax and nontax receipts.....	49.0	56.4	63.0	70.5	80.7	12.8	12.8	10.5	14.4
Income tax.....	24.8	30.9	35.5	38.8	45.0	15.8	15.1	9.2	16.0
Nontaxes.....	16.7	18.9	21.4	24.5	27.9	12.1	13.2	14.4	13.6
Other.....	6.1	6.7	7.0	7.4	7.9	8.3	5.2	5.0	7.5
Corporate profits tax accruals.....	8.5	11.8	11.7	13.0	11.9	18.5	6.7	11.0	-8.5
Indirect business tax and nontax accruals.....	122.3	141.0	149.8	158.0	171.4	9.9	6.3	6.0	7.9
Sales taxes.....	37.8	64.1	71.0	76.8	82.8	19.9	10.8	8.3	7.8
Property taxes.....	58.2	63.4	63.9	64.4	67.6	8.0	.9	.7	4.0
Other.....	12.3	13.5	14.0	17.7	21.2	9.9	10.8	17.0	20.2
Contributions for social insurance.....	18.5	22.1	24.8	28.1	31.5	12.1	11.3	14.5	11.9
Federal grants-in-aid.....	61.1	67.5	77.8	86.4	87.0	10.6	14.4	4.1	0.4
Addenda: Receipts, excluding selected law changes:									
Total.....	264.7	296.3	328.4	360.1	383.5	11.1	10.9	9.6	9.3
General own-source receipts.....	186.1	205.7	223.6	241.0	264.2	11.1	9.8	11.0	9.0

Contributions for social insurance increased 12 percent, compared with 14½ percent in 1979. Most of this deceleration was accounted for by a \$0.4 billion refund under the cash sickness (temporary disability insurance) program administered by the State of California; 80 percent of contributions paid by employees to the program during 1979 was returned during 1980.

Federal grants-in-aid increased 9½ percent, compared with only 4 percent in 1979, but 10½ percent and 14½ percent in 1977 and 1978. Much of the acceleration was in entitlement programs—Federal support for welfare benefits, medical vendor purchases, provision of food and home-heating for the needy, and training and human development programs. Grants for these programs increased 14 percent. Grants for capital purposes also increased strongly—11½ percent—despite a \$1.2 billion decline in local public works grants due to the running down of the 1977 program (only \$0.2 billion of an original \$6 billion remained unspent as 1980 ended). All other grants recorded an increase of less than 2 percent.

#### Expenditures

Expenditures increased 9½ percent in 1980, compared with 8½ percent in 1979 (table 2). Accelerations in purchases of structures and in direct relief transfer payments—the latter reflecting the 1980 slowdown in the economy—were major factors.

Total purchases again increased 9½ percent, but the composition of the increase differed from that in 1979. Purchases of structures increased 12 percent, up from 7½ percent. The 1980 increase was more than accounted for by prices, which increased 13 percent; real purchases of structures declined slightly. Other purchases of goods and services from business increased 10 percent, a little more than in 1979. Real purchases were flat. Compensation of employees increased 8½ percent in 1980, less than in 1979. Higher average compensation accounted for most of the 1980 increase. Real compensation increased only about 1 percent. About one-half of the increase in real compensation was due to an increase in employ-

ment. The other one-half was due to a shift from employment funded by the Comprehensive Employment and Training Act (CETA), which declined about 75,000, to permanent employment, which increased by about 140,000. (In the derivation of real compensation, a CETA employee's services are valued at \$7,000 in 1972 dollars, which is the estimated average compensation of an employee under the Public Employment Program of 1972, and a permanent employee's services are valued at about \$11,000; thus a shift of 75,000 from CETA to permanent employment is valued at about \$3 billion in 1972 dollars.)

In 1977 and 1978, CETA hiring by States and localities had been largely an addition to normal increases in employment (chart 5). In 1979, when CETA employment first declined, other employment accelerated, suggesting that many of those leaving CETA rolls became permanent employees.

In 1980, however, the further decline in CETA employment was not offset by larger-than-normal increases in permanent employment. Among the factors that contributed to the change in pattern from 1979 to 1980 are that: (1) the better qualified CETA employees, who are more easily absorbed into the permanent workforce, were "skimmed" off in 1979 as managers anticipated further

declines in CETA employment, and (2) by 1980 many governments had run down surpluses accumulated in 1977 and 1978, so that they were no longer able to finance larger-than-normal hirings.

Transfer payments to persons increased 11 percent, up from 7 percent in 1979. Welfare and related transfers, which react quickly to changes in the economy, accounted for most of the acceleration; they were up 14 percent after an increase of 3½ percent in 1979. Benefits from social insurance funds increased 11 percent, slightly less than in 1979, and other transfers increased 8½ percent, more than in 1979.

Interest received by government, which is netted against interest paid in the NIPA's, increased more rapidly than did most types of expenditures, thus holding down total expenditures growth. Dividends received by social insurance funds (which, until the recently published comprehensive revision of the NIPA's, were included with interest received) increased 4½ percent in 1980, more than in 1979, but significantly less than in 1977 and 1978. The lower rates of increase reflect a shift in the holdings of State and local government-administered retirement systems from stocks—i.e. dividend-paying investments—to interest-bearing investments.

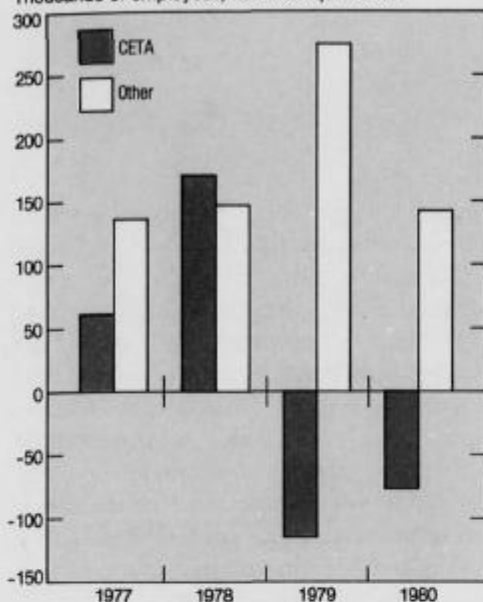
Table 2.—State and Local Government Expenditures, NIPA Basis

	Calendar years								
	Billions of dollars					Percent change			
	1976	1977	1978	1979	1980	1977	1978	1979	1980
<b>Expenditures</b> .....	251.2	270.0	285.4	324.4	354.8	7.5	10.3	9.7	9.3
Purchases of goods and services.....	222.9	250.6	278.2	306.9	326.7	7.6	11.4	9.6	6.7
Compensation of employees.....	183.8	144.0	157.5	172.3	187.4	8.9	9.8	9.4	8.7
Structures.....	83.4	31.0	37.5	40.3	45.2	-3.8	23.0	7.4	12.1
Medical vendor payments.....	14.3	15.7	17.1	19.4	21.5	10.6	9.4	13.3	10.6
Other purchases.....	84.3	30.9	67.1	73.9	81.8	10.3	22.1	16.1	10.3
Transfer payments to persons.....	27.4	20.7	33.9	35.0	38.9	7.8	30.3	3.0	10.0
Benefits from social insurance funds.....	11.3	12.5	14.1	15.9	17.2	10.6	13.3	12.3	10.3
Direct relief.....	12.9	18.4	12.8	14.1	18.8	4.7	3.2	3.3	38.3
Other.....	3.3	3.8	6.1	5.1	5.3	10.3	32.3	.8	3.4
Not interest paid.....	-3.8	-4.0	-8.2	-8.8	-12.8				
Interest paid.....	12.3	13.7	14.9	16.3	17.7	9.4	8.9	8.5	8.2
Less: Interest received by government.....	16.1	17.7	23.1	25.1	28.5	9.6	10.3	19.0	12.5
Less: Dividends received.....	.8	1.2	1.5	1.5	1.8	45.1	21.7	1.6	6.5
Subsidies less current surplus of government enterprises.....	-4.5	-6.1	-5.7	-6.3	-7.4				
Subsidies.....	.2	.3	.2	.3	.4	11.1	13.8	28.8	8.3
Less: Current surplus of government enterprises.....	5.0	5.4	5.9	6.7	7.7	6.4	11.7	11.7	15.5
Less: Wage accounts less disbursements.....	0	0	.2	-1	0				

### State and Local Government Employment: Change From Preceding Year

CHART 5

Thousands of employees, full-time equivalents



U.S. Department of Commerce, Bureau of Economic Analysis

81-2-5

### Fiscal position

With a surplus of \$2 billion on 1980, the State and local government sector excluding social insurance funds barely maintained the record of surpluses registered since 1975. These surpluses had been \$10 billion in 1977 and 1978 and \$3 billion in 1979. Over the past several years, certain mineral-wealthy States have recorded strong revenue growth, partly in response to sharply rising energy prices. In Texas, Alaska, and Louisiana, severance taxes and royalties increased sharply, as did corporate profits taxes in Louisiana and Alaska (Texas does not levy a corporate profits tax). These States have accumulated surpluses, while other States and localities in aggregate have moved into deficit.

This other-funds measure has usually registered a deficit; prior to 1972, when general revenue sharing funds accounted for much of the surplus, the last surplus was recorded in 1947. Because capital spending by government is combined with current spending in the summary NIPA presentations and because much of the capital spending by States and localities is funded by long-term bor-

rowing, the "normal" fiscal position of the other-funds measure has been a deficit.<sup>1</sup> The 1980 acceleration in capital spending helped explain the continued move toward deficit.

	1977	1978	1979	1980*
NIPA surplus or deficit (-):				
Total.....	28.1	20.0	26.7	28.8
Social insurance funds.....	17.9	20.0	23.9	26.9
Other funds.....	10.1	0.0	2.9	1.9

\* Preliminary.

### Outlook

In 1981, total receipts will increase at the same or at a slightly faster rate than in 1980. General own-source receipts are likely to increase faster, about 11 percent. The increase in personal income taxes is likely to accelerate. Several States now indexing these taxes—i.e., adjusting any or all three of the determinants of tax liability that are stated in dollar amounts (personal exemptions and deductions, and tax rate brackets) to reflect changes in the price level—are considering modification of the practice. Indexation had a modest dampening affect on overall 1980 growth; the intent of the modifications is to allow more rapid increases. If the economy improves in 1981, the decline in corporate profits taxes will end. It is likely that there will be fewer law changes limiting sales tax growth than there were in 1980.

Localities may allow property taxes to increase somewhat more rapidly than in 1980, as State legislatures (and the Federal Government as well) limit growth in grants-in-aid for local government use. The property tax increase will be held down by the Massachusetts action mentioned earlier, which will reduce total property tax accruals about \$0.4 billion in 1981. Other indirect business taxes will continue to increase rapidly, as energy prices continue to rise.

1. This and other characteristics of the surplus and deficit in the NIPA framework are discussed more fully in "State and Local Government Fiscal Position in 1978," in the December 1978 issue of the *Survey of Current Business*.

These faster increases in own-source revenue will be partly offset by a slower increase in Federal grants-in-aid. The State portion of general revenue-sharing is scheduled to stop in 1981, reducing grants by \$2.3 billion, and it appears that the Administration will attempt to curb growth in grants programs supporting construction of highways, mass transit, and water treatment plants. Grants for CETA employment are likely to be further reduced, if not eliminated, in 1981. For the year as a whole, grants increases are unlikely to exceed 4-5 percent.

Increases in expenditures will probably remain under 10 percent. Construction will probably increase very little, as grants for capital purposes are cut back. Further reductions in CETA employment will probably limit compensation growth, and some improvement in the economy will allow welfare transfers to increase more slowly. In California, State spending may have to be reduced below current levels.

Following the passage of Proposition 13 in 1978, the State used its large accumulated general fund surplus to help finance local government spending, especially for welfare and education. (See "Proposition 13: One Year Later," in the November 1979 *SURVEY OF CURRENT BUSINESS*.) That surplus, which was \$4 billion in June 1979, declined to less than \$1 billion as of January 1981; almost all of that surplus is reserved for an "economic uncertainty" contingency fund. Unless increases in major State receipt categories accelerate sharply in the next few months, State support for local operations will have to be reduced.

The 1981 surplus on the NIPA basis will be somewhat larger than in 1980—about \$32 billion. The social insurance funds will show a surplus of about that amount, and the other funds will be in approximate balance. Several of the points mentioned—specifically, smaller increases in welfare transfers, stability of corporate profits taxes, and larger increases in personal income taxes—rest on an assumption of some improvement in the economy. In the absence of such an improvement, the other-funds measure will move into deficit.